IN THE

# Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-731

SUN OIL COMPANY, GENERAL CRUDE OIL COMPANY,
M. H. MARR, CONTINENTAL OIL COMPANY,
*Petitioners,*

v.

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
PHILADELPHIA GAS WORKS DIVISION OF UGI CORPORATION,
TEXAS EASTERN TRANSMISSION CORPORATION,
FEDERAL POWER COMMISSION,
*Respondents.*

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT*

## BRIEF FOR RESPONDENT TEXAS EASTERN TRANSMISSION CORPORATION IN LIMITED OPPOSITION

J. EVANS ATTWELL
P. M. SCHENKKAN
Vinson, Elkins, Searls,
Connally & Smith
2100 First City National
Bank Building
Houston, Texas 77002

JACK D. HEAD
P. O. Box 2521
Houston, Texas 77001

*Attorneys for Texas Eastern Transmission Corporation*

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## QUESTION PRESENTED

The petition filed in this case presents two questions. Respondent Texas Eastern Transmission Corporation ("Texas Eastern") opposes Petitioners' application for a writ of certiorari with respect to the second "Question Presented" by Petitioners.[1] Texas Eastern submits that this question is more accurately stated as follows:

[1] Petitioners' first "Question Presented" asks this Court to review the decision of the court below ordering the Federal Power Commission to prescribe refunds by Petitioners based upon an area rate of 18.5¢ per thousand cubic feet (Mcf), rather than the higher rates established by the Commission in Opinion No. 598, 46 FPC 86 (1971). Texas Eastern takes no position on Petitioners' request for a writ of certiorari on this question.

Did the court below err in holding that the Federal Power Commission had improperly implemented its "limited power to raise prices for natural gas above those contractually fixed by the parties."[2]

## STATEMENT

### A. Background

This case concerns Petitioners' 1958 agreement to sell Texas Eastern their leasehold interests in the Rayne Field, Acadia Parish, Southern Louisiana. The contract provided an aggregate sales price of $134,395,000, to be paid in installments over a sixteen-year period ending in 1975. Under the contract, after 1975 Texas Eastern would obtain gas throughout the remaining life of the Field (then estimated to be 1986) free of cost except for royalties, severance taxes and operating expenses. Although Rayne Field gas began to flow into Texas Eastern's system in 1959, the Rayne Field sale has been in continuous litigation ever since.[3]

On one previous occasion, the Rayne Field sale has been before this Court. In *United Gas Improvement Co.* v. *Continental Oil Co.*,[4] this Court decided an important question of federal law, holding that the Federal Power Commission possesses jurisdiction over the sale to an interstate pipeline of leasehold interests in proven gas reserves in place. The Court disclaimed any intention of reviewing "the pro-

[2] Petitioners' Appendix – hereinafter "App." – A, at p. A54.

[3] *See Texas Eastern Transmission Corp.*, 21 FPC 860 (1959), *rev'd sub nom. Public Serv. Comm'n* v. *FPC*, 287 F.2d 143 (D.C. Cir. 1960); *Texas Eastern Transmission Corp.*, 29 FPC 249 (1963), *rev'd sub nom. M. H. Marr* v. *FPC*, 336 F.2d 320 (5th Cir. 1964), *rev'd sub nom. United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965); *Texas Eastern Transmission Corp.*, Opinion No. 565, 42 FPC 376 (1969), Opinion No. 565-A, 44 FPC 1079 (1970), Order Denying Rehearing, 44 FPC 1471 (1970), *aff'd in part and rev'd in part sub nom. Public Serv. Comm'n* v. *FPC*, App. A., A1-A135 (D.C. Cir. 1974).

[4] 381 U.S. 392 (1965).



priety of the Commission's disposition of the [present] case following its assertion of jurisdiction."[5] Here, the court below held that the Commission's subsequent disposition of the present case, though fundamentally sound in approach, erred in certain particulars. Petitioners seek to attack the court below on two of its findings of error in the Commission's disposition.

### B. Proceedings Before the Commission

Following this Court's jurisdictional holding, Petitioners applied to the Commission for certificate authorization of their leasehold sale in accordance with the terms of their contract with Texas Eastern. In response to these applications, the Commission issued Opinion No. 565 (App. F, pp. F1-F103), approving the lease-sale subject to conditions making it substantially closer in nature to a conventional gas sale. In a conventional sale, the parties agree on a price for each unit of gas to be delivered. When certification of a conventional sale is sought, the Commission performs its statutory obligation to protect interstate consumers against excessive prices by conditioning its certificate so as to limit the initial unit price of the gas to a just and reasonable rate, or to a price in line with other analogous transactions, pending formal establishment of a just and reasonable rate. But the Commission found that in a lease-sale transaction it would be impossible to ascertain the cost of the gas per unit until the field had been depleted. In addition, the Commission found that the Rayne Field lease-sale arrangement would apparently produce a higher unit cost than would a conventional sale at the applicable just and reasonable price per Mcf (*id.* at p. F20). Accordingly, the Commission decided to "conventionalize" the Rayne Field sale.

[5] 381 U.S. at 399.

In order to "conventionalize" Petitioners' sale, the Commission attached a number of conditions to their certificates. Among them was the condition that Texas Eastern pay the total agreed purchase price of $134,395,700 at a rate of 18.5¢ per Mcf of production. (App. F at p. F20). The Commission understood that this would entail a longer payment period than originally contemplated (*id.*). Commissioners Carver and Brooke dissented. They noted that "conventionalizing" the transaction to provide instead that Texas Eastern would pay 18.5¢ per Mcf as long as deliveries continued "might require the pipeline to pay more, ultimately, than the 1959 contract provided" (*id.* at F88), but that the approach actually adopted by the Commission provided for less consideration that the contract provided, since the same face amount was to be paid off over a longer period (*id.* at F88-89).

On rehearing, the Commission issued Opinion No. 565-A, which reaffirmed its "conventionalization" approach but modified some of its conditions (App. G, pp. G1-G48). In particular, the Commission decided to abrogate the $134 million lease-sale contract price, requiring instead that Texas Eastern continue to make payments to Petitioners for each unit of gas produced until exhaustion of the Field (App. G at p. G4). Chairman Nassikas and Commissioner Bagge voted to do this "in the interest of bringing about an equitable result" (*id.* at G4), and "to do equity to the parties" (*id.* at G11). "Reluctantly," Commissioners Carver and Brooke concurred in this decision, even though they recognized again that it created "more than a possibility" that Texas Eastern and its customers would ultimately pay an amount that would "greatly exceed" the original contract price, discounted to current dollars (*id.* at G38-39). In their view, this was "preferable to the confiscation involved in assuming that a dollar paid over two years is equal to a dollar paid in one year. Our concurrence goes no further"



(App. G at p. G31). Commissioner O'Connor, the fifth Commissioner, dissented. Emphasizing that his colleagues' "differences of opinion largely focus on who shall have priority in equity" (*id.* at G21), he attacked the majority's decision to allow Petitioners as much as an additional $52,141,000 above the contract price (*id.* at G27).

By a three-to-two vote, the Commission subsequently denied rehearing of Opinion No. 565-A (*see* App. H, pp. H1-H7). But Commissioner O'Connor, who cast the decisive vote against rehearing, issued a concurring opinion arguing for a middle ground. Accepting that "the time value of money must be considered as an element in reaching an equitable disposition of this case," he contended that the $134 million purchase price should be increased *only* by the amount necessary to compensate Petitioners for the additional payment time resulting from the Commission's decision to require payment by the Mcf produced (*id.* at H3-H4). Inclusion of this interest component, he pointed out, would best harmonize "with the intent of the parties as the lease-sale agreement was drafted" (*id.* at H4).

Commissioners Carver and Brooke, dissenting, attempted to "withdraw our reluctant concurrence" in Opinion No. 565-A, in order to deprive of force and effect that opinion's requirement that payment be made over the life of the reserves (*see id.* at H7). Although they adhered to their previous position that the lease-sale should be certificated unconditionally, they recognized that within the conventionalization framework Commissioner O'Connor's suggestion would achieve the goal of preserving the parties' agreement on the sale price (*see id.* at H6-H7).

### C. The Decision Below

After subjecting the Commission's orders to searching and exhaustive analysis, the court below affirmed its deci-

sion that the unmodified lease-sale transaction failed to meet the public convenience and necessity standard and would have to be "conventionalized" (A33-A48).[6] However, the court found certain aspects of the Commission's "conventionalization" conditions impermissible, among them its requirement that Texas Eastern continue to pay Petitioners throughout the life of the Field, without regard to the maximum contract price. The court below based this aspect of its decision on this Court's consistent declaration that "the regulatory system created by the [Natural Gas] Act contemplates abrogation of [natural gas companies' contractual] agreements only in circumstances of unequivocal public necessity."[7] The court pointed out that the Commission's decision to eliminate the contract price between Petitioners and Texas Eastern was nowhere predicated on a finding that "unequivocal public necessity" required such a change or that it was essential to the conventionalization of the lease-sale arrangement. Instead, the Commission merely regarded it as "equitable" to remove the $134 million contract price ceiling in order to adjust the difference in time value of the payments received. This did not amount to a finding that the contract price was "so low as to adversely affect the public interest."[8] Nor did the Commission find that "financial or other difficulties . . . required the Commission to relieve the producers . . . from the burdens of their contractual obligations."[9] In fact, "the Commission's alteration of the stipulated aggregate price has not been shown to serve any facet of the public interest at all" (App. A at p. A68).

[6] The court first rejected arguments that the changes of position expressed in the dissent of Commissioners Carver and Brooke to the Commission's order denying rehearing of Opinion No. 565-A vitiated the latter, thus restoring Opinion No. 565. The court held that the only effect of the Commission's order was to deny rehearing of Opinion 565-A, thus leaving it unaffected (*id.* at A32).

[7] *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968), citing *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956).

[8] App. A at p. A68, quoting *FPC* v. *Sierra Pac. Power Co.*, 350 U.S. 348, 355 (1956).



The court below decided, however, that the Commission's previous decision in Opinion No. 565, retaining the aggregate contract price but spreading payments over a longer period of time than provided by the contract, violated the same principles: it deprived the Petitioners of "the *quid pro quo* for which they contracted" (*id.* at A70), by diminishing the value to them of the face amount of the consideration. It found that, given these principles and the fact that the Commission had repeatedly held conventionalization to be necessary in the public interest, the only alternative legally available to the Commission was to order an increase in Texas Eastern's payments beyond the face amount provided in the contract, but only by an amount equal to the time value of the money to be paid on the Commission's extended payment schedule.[10] In favor of this result, the court advanced the same argument used by Commissioners O'Connor, Carver and Brooke (*see* App. H at pp. H4-H7). According to the court, it "would confer on the producers the full equivalent of their contract price, and would impose on Texas Eastern no more than the equivalent of its contract cost . . ." (App. A at p. A71). Moreover, this Court's requirement that contractual agreements voluntarily devised must govern, absent a showing that circumstances of unequivocal public necessity otherwise require, would be satisfied (*id.*).

[9] App. A at p. A68, quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 822 (1968).

[10] The court below held that, in lieu of remand for this purpose, its judgment would incorporate such a modification of the Commission's disposition (App. A at p. A71).

D. **Summary of Texas Eastern's Position**

Throughout this extraordinarily protracted litigation Texas Eastern has had two objectives: to secure the Rayne Field reserves for its customers at the lowest possible price, and to recover the costs it has incurred in purchasing Petitioners' interests in those reserves. Texas Eastern believes that, at the aggregate contract price of $134 million, it has attained the first objective.[11] For the sake of both objectives, Texas Eastern would have preferred that the Commission approve the leasehold transaction in its entirety. But the Commission substantially modified the leasehold transaction by attaching conditions to the certificates it issued Texas Eastern and Petitioners, including the condition that eliminated the $134 million ceiling on Texas Eastern's liability to Petitioners, established by the contract.

This condition would deny Texas Eastern an opportunity to recover prudently incurred costs. From the beginning, Texas Eastern has taken care to avoid penalizing present day consumers with costs already incurred but properly attributable to future consumers. Accordingly, it has spread the total cost of its investment, payable in full under the contract by 1975, over the life of the Rayne Field, originally estimated to end in 1986. That is, Texas Eastern charges current consumers only their amortized share of the contract price. As a result, a very substantial portion of the payments Texas Eastern has made to Petitioners remains on Texas Eastern's books.[12] This unamortized balance represents Texas Eastern's investment in the gas to be produced after Petitioners have been paid the total contract consideration. If, however, Texas Eastern is required to continue to pay Petitioners until the exhaustion of the reserves, Texas Eastern will never be able to amortize this portion of its investment. The Commission's condition would invalidate the assumption upon which amortization was based — the assumption that the unamortized portion of the contract price could be charged to the consumers of gas produced after Petitioners had been paid in full.

[11] One Commissioner has twice characterized the Rayne Field transaction as yielding "*the lowest cost of gas of this vintage*, including gathering and transmission costs, *ever delivered to consumers.*" (App. G at p. G21, App. H at p. H5) (emphasis added). Two others have called this sale "a bargain situation for consumers" (App. G at p. G48).

[12] According to the record below, as of 1970 almost $28 million had been paid to Petitioners but not included in rates charged to consumers of Rayne Field gas (R. 6811).



The opinion of the court below affirmed the Commission's decision to conventionalize the lease-sale transaction. But it removed from that decision the features that might have compelled Texas Eastern to seek a writ of certiorari from this Court, including the Commission's elimination of the contract price ceiling. The court remanded to the Commission the other issues that will determine Texas Eastern's ultimate ability to recover its investment (*see* App. A at p. A134-135 and App. C at p. C22 & fn 108). Accordingly, while remaining of the view that unconditional certification would have served the public interest, Texas Eastern does not seek review of the decision below.[13]

Texas Eastern's remaining stake in the present controversy is the risk of a multi-million dollar increase in its

[13] No question is presented concerning the refusal of the court below to grant unconditional certification of the lease-sale. Each of the two questions which Petitioners say are presented here concerns a specific, limited aspect of the Commission's conditions, as modified by the court below. Neither addresses the underlying decision to conventionalize. *See* Petition at p. 2. In the last paragraph of their petition, however, Petitioners imply that they seek a full remand and a *de novo* Commission decision on conventionalization. *See id.* at p. 24. In view of this Court's Rules, Texas Eastern assumes that this suggestion does not affect the scope of review sought. *See* Rule 23(1)(c). However, Texas Eastern does continue to believe that the leasehold sale of Rayne Field reserves should have been certificated unconditionally.

ultimate financial liability on the Rayne Field transaction. As the court below noted, this increase could not be precisely calculated in the course of a Section 7 certification proceeding, if at all (App. A at p. A65). It depends upon the life of the Field and on the outcome of future ratemaking by the Commission. But the minimum estimates of three commissioners range from nearly $18 million to more than $52 million (*id.*). In any event, Texas Eastern contracted for the security of a fixed price, as the Petitioners themselves have previously argued (*see id.* at A46), and based its accounting on the assumption of a fixed price. Texas Eastern accepts that the Petitioners should not "receive less than the *quid pro quo* for which they contracted" (*id.* at A70, A71 & fn. 348). The decision of the court below, ordering adjustment of the contract price to take account of the time value of money, gives Petitioners that assurance. Texas Eastern asks only that it not be required to risk having to pay Petitioners *more* than the quid pro quo for which they contracted.

## ARGUMENT

### 1. The Question Presented Involves Virtually Unique Facts

This Court decided the only new question in this protracted litigation of general interest throughout the natural gas industry when it held that the Commission had jurisdiction to review sales to interstate pipelines of leasehold interests in proven reserves.[14] No one disputes that this decision effectively foreclosed the likelihood that the Commission or the courts will have to consider more lease-sale situations.[15] Thus, though of considerable financial interest to the parties to this case, resolution of the question whether in this case the Commission properly exercised its limited power to raise natural gas prices above those contractually

[14] *United Gas Improvement Co.* v. *Continental Oil Co.*, 381 U.S. 392 (1965).

[15] *Cf.* App. F at p. F68 (Carver, Comm'r, dissenting).



agreed upon by the parties to a leasehold sale will not have wide precedential value. Petitioners make no attempt to argue to the contrary.

### 2. The Question Presented Involves the Application of Settled Law

The court below held that the Commission's deviations in Opinions No. 565 and 565-A from the value of the consideration bargained for by the parties violate settled law. In *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*[16] and *FPC* v. *Sierra Pacific Power Co.*[17] this Court denied that the Natural Gas Act and the Federal Power Act conferred upon the Commission any general power to set natural gas prices above those contractually fixed by the parties. In the *Permian Basin Area Rate Cases*[18] this Court explained under the Natural Gas Act the Commission could raise producers' contract prices "only in circumstances of unequivocal public necessity."[19] The principles have repeatedly been applied, and have never been challenged. Petitioners do not challenge them. Nor do Petitioners assert that their application by the court below conflicts with any decision of this Court or of any circuit court.

Petitioners do, however, intimate that these principles, while valid in the context of Sections 4 and 5 of the Natural Gas Act, should not apply when the Commission invokes its Section 7 power to confer and condition certification. The court below held that this Court's *CATCO* decision[20] makes it clear that the Commission cannot increase the contractually agreed prices absent a finding of compelling public necessity in Section 7 proceedings any more than in proceedings under Sections 4 and 5. Petitioners summarily

[16] 350 U.S. 332 (1956).

[17] 350 U.S. 348 (1956).

[18] 390 U.S. 747 (1968).

[19] *Id.* at 822.

[20] *Atlantic Ref. Co.* v. *Public Serv. Comm'n*, 360 U.S. 378 (1959).

dismiss the court's reading of *CATCO* as "erroneous". Without citation of authority they assert that it is "not reasonable to assume" that the Commission's power to condition a certificate so as to raise the contract price should be limited to circumstances in which public necessity requires such a change. But the very portion of the Natural Gas Act upon which Petitioners rely, Section 7(e), provides in pertinent part:

> The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions *as the public convenience and necessity may require* [emphasis added].

That is, the statute on its face confines the Commission's Section 7(e) certificate-conditioning power to the same circumstances of unequivocal public necessity within which this Court has found the Commission's Sections 4 and 5 contract-modification power to be limited.

### 3. The Court Below Correctly Decided the Question Presented

After arguing that the Commission can raise their contract price even without attempting to show that the public interest requires this change, Petitioners change their ground and argue that the Commission made the necessary finding. They allege that, contrary to the opinion of the court below, the Commission "*expressly*" found that its condition extending Texas Eastern's obligation to pay over the life of the Rayne Field reserves was "*essential* to conventionalization of the lease-sale arrangement." (Petition at p. 22, emphasis added). In fact, the Commission neither expressly nor implicitly so found. The Commission imposed its condition abrogating the lease-sale contract price "in the interest of bringing about an equitable result" (App. G at p. G4).



Indeed, the authors of the prevailing Commission opinion could not even muster a majority for the proposition that it was "only equitable" (App. G at p. G11) for Petitioners to receive more than they bargained for. Commissioners Carver and Brooke would have prefered to approve the lease-sale arrangement as originally proposed, without conditions. As a second choice, they advocated adjusting the apparent contract price to take account of the time value of money, as the court below subsequently decided to do. Only because they could not find a third vote at that time for either of these alternatives did they supply Chairman Nassikas and Bagge with reluctant support for the condition invalidated by the court below (*see id.* at G30-G31). In short, two members of the Commission that issued Opinion No. 565-A thought that equity called for the condition invalidated by the court below, and another two found this condition, though distasteful, preferable to the condition imposed in Opinion No. 565. No one found it necessary, essential, or required in the public interest. As stated by the court below, "the Commission's alteration of the stipulated aggregate price has not been shown to serve any facet of the public interest at all" (App. A at p. A68).

Petitioners contend that for two reasons the public interest does require Texas Eastern to pay them for each Mcf of gas produced from the Rayne Field until its reserves are exhausted, no matter how much this may increase the aggregate consideration that Texas Eastern contracted to pay and Petitioners agreed to accept for this gas. Their counsel's post hoc rationalizations, which were not the basis of the agency decision in question, would be unacceptable on judicial review in any event.[21] Moreover, Petitioners' "undisputed reasons" would not support a finding that the

[21] *Burlington Truck Lines* v. *United States*, 371 U.S. 156, 168-69 (1962); *Texas Gas Transmission Corp.* v. *Shell Oil Co.*, 363 U.S. 263, 270 (1960); *SEC* v. *Chenery Corp.*, 332 U.S. 194, 196 (1947).

public interest required the challenged life-of-reserves condition even if the Commission, rather than Petitioners, had advanced them for this purpose.

First, the $134 million lease-sale agreement aggregate price would of course be of less value to Petitioners than the contract contemplated to the extent that they receive payment over a longer period than the agreement provided. But the obvious solution, recognized by three Commissioners and utilized by the court below, is to increase the $134 million aggregate by that amount, and only that amount, required to compensate Petitioners for the additional delay in payment. The need to avoid giving Petitioners substantially less than they bargained for can constitute no reason, and certainly not one of compelling public necessity, for paying Petitioners substantially more than they bargained for.

Second, it is obviously true that holding Petitioners to the aggregate price they bargained for, whether or not adjusted for changes in the timing of payment dictated by "conventionalization", would not permit them to receive payment throughout the life of the Field, as would be the case in a conventional sale. But the fact that payment over the life of the reserves is inherent in a conventional sale does not begin to show that similar payment is required by the public interest as a condition of certification of a lease-sale. Petitioners are reduced to arguing that because they would benefit by abrogation of the price term of their contract abrogation must be required in the public interest.



## CONCLUSION

For the foregoing reasons the decision of the court below, reversing the Commission's order requiring Texas Eastern to pay Petitioners until the Rayne Field reserves are exhausted, presents no question warranting review by this Court. Insofar as the petition for a writ of certiorari presents this question, it should be denied.

Respectfully submitted,

J. Evans Attwell
P. M. Schenkkan
Vinson, Elkins, Searls,
Connally & Smith
2100 First City National
Bank Building
Houston, Texas 77002

Jack D. Head
P. O. Box 2521
Houston, Texas 77001

*Attorneys for Texas*
*Eastern Transmission*
*Corporation*